BEFORE THE
NORTH CAROLINA UTILITIES COMMISSION

In the Matter of: Global NAPs North Carolina, Inc. Petition for Arbitration Pursuant to Section 252(b) of the Telecommunications Act of 1996 to Establish an Interconnection Agreement with Verizon South, Inc. f/k/a GTE South Incorporated	Docket No. P-1141, Sub 1

DIRECT TESTIMONY
OF TERRY HAYNES ON BEHALF OF
VERIZON SOUTH INC.

MAY 14, 2002

I. WITNESS BACKGROUND AND OVERVIEW

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND POSITION WITH VERIZON.

A. My name is Terry Haynes. My current business address is 600 Hidden Ridge, Irving, Texas 75015. I am a manager in the State Regulatory Policy and Planning group supporting the Verizon states formerly associated with GTE. I am testifying here on behalf of Verizon South Inc. ("Verizon").

Q. PLEASE DESCRIBE YOUR EDUCATIONAL AND PROFESSIONAL BACKGROUND.

A. I received a Bachelor of Arts Degree in Philosophy from the University of South Carolina in 1973. Since 1979, I have been employed by Verizon and its predecessor companies. I have held positions in Operations, Technology Planning, Service Fulfillment and State and Federal Regulatory Matters.

Q. PLEASE DESCRIBE THE PURPOSE OF YOUR TESTIMONY.

A. I will address Issues 3 and 4 presented in GNAPs' Petition for Arbitration, including the disputed contract language and GNAPs witness Lundquist's Direct Testimony associated with those issues. These issues, as stated in GNAPs Petition, are:

Issue No.	Statement of Issue	Disputed Contract Sections Related to Issue
Issue 3	"Should Verizon's local calling area boundaries be imposed on GNAPs or may GNAPs broadly define its own local calling area?"	Glossary §§ 2.34, 2.47, 2.56, 2.75, 2.83, 2.91; Interconnection Attachment §§ 2, 6.2, 7.1, 7.3.4 and 13.3.
Issue 4	"Can GNAPs assign to its customers NXX codes that are 'homed' in a central office switch outside of the local calling area in which the customer resides"	Glossary §§ 2.34, 2.47, 2.56, 2.75, 2.83, 2.91; Interconnection Attachment §§ 9.2 and 13.

In addition to discussing these issues, I will briefly respond to Mr. Lundquist's testimony on intercarrier compensation for internet service provider (ISP) traffic.

Q. PLEASE SUMMARIZE YOUR TESTIMONY.

A. With respect to Issue 3, Verizon agrees that GNAPs should remain free to define its retail local calling areas as broadly as it likes. What GNAPs cannot do, however, is unilaterally undermine Verizon's North Carolina's toll and access charge regime by defining the local calling area for purposes of reciprocal compensation obligations. Verizon's tariffed local calling areas should continue to be the basis for assessing reciprocal compensation. This is the simplest and most competitively neutral approach.

With respect to Issue 4, is GNAPs is permitted to assign telephone numbers to end users located outside of the rate center to which those numbers are homed, Verizon's proposed contract language ensures that GNAPs cannot impermissibly alter the appropriate intercarrier compensation by virtue of GNAPs' assignment of these "virtual NXX" codes. Because GNAPs' virtual NXX traffic is not local in nature, reciprocal compensation does not apply to this traffic.

Finally, Mr. Lundquist's proposal for the Commission to adopt a TELRIC-based reciprocal compensation for ISP traffic is at odds with governing federal law and sound policy.

II. ISSUE 3:

Q. MR. LUNDQUIST STATES THAT "VERIZON SOUTH HAS TAKEN THE POSITION THAT GLOBAL NAPS' LOCAL CALLING AREAS SHOULD MIRROR VERIZON'S LOCAL CALLING AREAS." LUNDQUIST DIRECT AT 2. IS THAT TRUE?

A. No. Both GNAPs' Petition and Mr. Lundquist's Testimony misrepresent Verizon's position and try to cloud the real dispute at issue. Verizon has never proposed to limit GNAPs' ability to define its own local calling areas for retail purposes. The nature of the dispute, rather, is ***only*** how the interconnection contract should define the local calling area for purposes of assessing reciprocal compensation. Regardless of what local calling area is used for reciprocal compensation purposes, GNAPs will remain free to market any local calling scopes it wishes, as it can today.

Q. WHAT IS THE BASIS FOR DEFINING RECIPROCAL COMPENSATION OBLIGATIONS TODAY?

A. Interconnection contracts typically define reciprocal compensation obligations with reference to the incumbent local exchange carrier's tariffed local exchange areas. Verizon recommends maintaining this *status quo*, for the reasons I explain below.

Q. WHAT CHANGE DOES GNAPS PROPOSE?

A. GNAPs contends that it "should be allowed to broadly define its own local calling area, possibly as large as a single LATA." GNAPs Petition at 17; *see also* GNAPs' proposed definitions of "Reciprocal Compensation Traffic," Glossary § 2.74; "Extended Local Calling Scope Arrangement," Glossary § 2.34; "Measured Internet Traffic," Glossary § 2.56; "IXC (Interexchange Carrier)," Glossary § 2.47; and "Toll Traffic," Glossary § 2.90. As noted, Verizon does not oppose allowing GNAPs to define its own retail local calling areas, but GNAPs seeks to determine reciprocal compensation obligations based on whether the originating carrier assesses toll charges on the customer originating the call. What this means, in practical terms, is that GNAPs could designate the entire LATA (or, for that matter, the entire nation) as its local calling area and avoid Verizon's tariffed access charges that apply to intraLATA toll calls today. In addition, GNAPs would bill Verizon for reciprocal compensation for any Verizon-originated call that GNAPs terminated within the LATA (or whatever region GNAPs designated as a local calling area). This extreme proposal would have disastrous policy consequences.

Q. IN THAT REGARD, WHAT CONSIDERATIONS SHOULD GUIDE THE COMMISSION'S RULING ON THE LOCAL CALLING AREA FOR PURPOSES OF DETERMINING INTERCARRIER COMPENSATION OBLIGATIONS?

A. The interconnection agreement's designation of the local calling area for reciprocal compensation purposes must: (1) avoid undermining the advancement and preservation of universal service, (2) be competitively neutral, and (3) be administratively easy to implement. Continued use of Verizon's Commission-approved local calling areas to define intercarrier compensation obligations serves these objectives. In contrast, none of

these objectives will be met if the Commission adopts GNAPs' proposal to allow the originating carrier to define the local calling area for intercarrier compensation purposes.

Q. WHAT WOULD BE THE CHIEF CONSEQUENCE OF ADOPTING GNAPS' PROPOSAL ?

A. GNAPs' proposal would obliterate the local/toll distinction reflected in Verizon's tariffs and that this Commission has maintained for decades. This distinction is not simply a historical accident or anachronism, as Mr. Lundquist posits. It is, rather, related to deliberate policy choices made by this Commission and North Carolina's commitment to universal service (reflected in NC General Statute section 62-110(f)(1)). Access and toll services are priced above cost today in order to provide support to basic local rates, which are priced below their relevant costs. This system of implicit subsidies serves the Commission's key policy objective of maintaining and promoting universal service.

What GNAPs proposes, in effect, is unilateral access ***and*** toll reform—that is, the elimination of toll services for end users that call GNAPs' customers, thus taking toll rates to zero. All of this would occur without any recognition of the subsidies implicit in those toll rates, as well as in the switched access charges that are either directly or implicitly associated with those toll calls. This proposal has repercussions far beyond the scope of this docket. If the Commission wishes to consider the radical policy shift GNAPs proposes, it should do so in a generic proceeding in which all interested parties can participate, rather than in an arbitration between two parties.

Q. WHY ISN'T GNAPS' PROPOSAL COMPETITIVELY NEUTRAL?

A. Defining the entire LATA as the local calling area, as GNAPs apparently intends to do, would place Verizon and the interexchange carriers ("IXCs") at a competitive disadvantage with regard to intraLATA toll calling. GNAPs' calls within the LATA would be termed "local" and subject to reciprocal compensation. But an intraLATA call that involves an IXC would still be subject to access compensation rules. Applying different intercarrier compensation rules to the same type of calls would give GNAPs a significant, artificial competitive advantage in pricing its intraLATA calls (regardless of whether it deems them local calls or toll calls) versus pricing based on the cost structures that the IXC and Verizon (through the Commission's imputation policy) face.

Q. PLEASE EXPLAIN FURTHER HOW ACCESS CHARGES ARE ASSESSED ON INTRALATA CALLS TODAY.

A. Access charges are applied to intraLATA toll calls as between a local carrier and an IXC and as between two local carriers.

For intraLATA toll calls carried by IXCs, the IXC pays the originating ILEC an originating access charge (the major components of which are an end-office switching charge, a transport charge, a carrier common line charge, an interconnection charge and a tandem switching charge) and the IXC pays the terminating ILEC a similar terminating access charge. In Verizon's territory, the net sum of originating and terminating charges averages about $0.08 per minute, which the IXC recovers through its toll charges to its customer.

Q. DO THESE SAME ACCESS CHARGE STRUCTURES APPLY WHEN A CLP (RATHER THAN AN ILEC) ORIGINATES OR TERMINATES AN IXC'S INTRALATA TOLL CALL?

A. Yes, access charges were developed to address compensation between all local exchange carriers and IXCs when those carriers collaborate to complete long distance calls. Verizon will bill the IXC access charges for whichever end of the call Verizon handles (originating or terminating). The CLP, likewise, can be expected to charge the IXC an access rate for the other end of the call. The following table depicts the various end-user and intercompany charges for intraLATA toll that occur under today's set of rules:

Table 1

Compensation Between (1) ILECs or CLPs and (2) IXCs When They Collaborate to Complete IntraLATA Toll Calls
(Current Rules)

ILEC or CLP Originating Call	**IXC**	**ILEC OR CLP** Terminating Call
Charges the IXC for originating access	Charges the end user for toll service	Charges the IXC for terminating access

Q. WHAT HAPPENS TODAY WHEN THERE IS NO IXC INVOLVED, AND THE ILEC AND CLP COLLABORATE TO COMPLETE AN INTRALATA TOLL CALL?

A. When an ILEC and an CLP collaborate to complete an intraLATA toll call (excluding toll free services such as 800/888), the following compensation flows apply:

Table 2

Compensation Between ILECs and CLPs When They Collaborate to Complete IntraLATA Toll Calls
(Current Rules)

ILEC Originating Call Charges the end user for toll service	**CLP Terminating Call** Charges the ILEC for terminating access
CLP Originating Call Charges the end user for toll service	**ILEC Terminating Call** Charges the CLP for terminating access

Q. HOW WOULD DEFINING THE LATA AS THE LOCAL CALLING AREA FOR RECIPROCAL COMPENSATION PURPOSES FAVOR GNAPS RELATIVE TO OTHER CARRIERS?

A. The FCC requires the reciprocal compensation rate to equal the economic cost of the underlying facilities used to terminate traffic; this rule necessarily precludes inclusion of implicit support for universal service objectives. So if the entire LATA were GNAPs' local calling area for reciprocal compensation purposes, GNAPs' new cost structure for what was access traffic would be: Total Direct Cost of a GNAPs Call = GNAPs' Originating Facility and Transport Costs plus the ILEC's Reciprocal Compensation Charge. Thus, whereas GNAPs today would pay something toward universal service support through the access charge structure, it would pay nothing if the LATA is the local calling area for assessing reciprocal compensation—again, because reciprocal compensation, unlike access charges, does not include any implicit support for the advancement and preservation of universal service. Because significant amounts of such support continue to exist in the IXCs' toll cost structure and in the ILECs' imputed toll cost structure, the IXCs and the ILECs are artificially disadvantaged in their provision of toll vis a vis GNAPs.

Q. WILL GNAPS' PROPOSAL CREATE NEW ARBITRAGE OPPORTUNITIES?

A. Yes. GNAPs' approach enhances its opportunities to arbitrage Verizon's existing rate structures. Notice that when ILECs or CLPs collaborate with an IXC to complete long-distance calls under the LATA-wide reciprocal compensation scenario, the inter-company compensation with the IXC would be the same as it is now:

Table 3
Compensation Between (1) ILECs or CLPs and (2) IXCs When They Collaborate to Complete IntraLATA Toll Calls
(LATA-wide Reciprocal Compensation Scenario)

ILEC or CLP Originating Call	**IXC**	**ILEC OR CLP** Terminating Call
Charges the IXC for originating access	Charges the end-user for toll service	Charges the IXC for terminating access

In contrast, when an ILEC and an CLP collaborate to complete what was previously an intraLATA toll call (excluding toll free services such as 800/888), terminating access charges would be replaced with a reciprocal compensation charge (which is significantly less than access charges):

Table 4
Compensation Between ILECs and CLPs When They Collaborate to Complete IntraLATA Toll Calls
(LATA-wide Reciprocal Compensation Scenario)

ILEC Originating Call Charges the end-user for toll service	**CLP Terminating Call** Charges the ILEC the reciprocal compensation rate
CLP Originating Call Charges the end-user for toll service	**ILEC Terminating Call** Charges the CLP the CLP's reciprocal compensation rate

The point is that competitive neutrality must be evaluated by looking at all the participants in the marketplace, not just a selected few. GNAPs' proposal ignores this simple fact. It would confer upon itself an artificial cost advantage because GNAPs, unlike the IXCs and the ILECs, would pay nothing to support universal service. Nothing about GNAPs' proposal is competitively neutral.

Q. DOES GNAPS' VIRTUAL NXX PROPOSAL FURTHER JEOPARDIZE COMPETITIVE NEUTRALITY AND UNIVERSAL SERVICE SUPPORT?

A. Yes. Later, I address GNAPs' virtual NXX proposal in greater detail, but it is worth note here that it exacerbates the competitive neutrality and universal service problems that I have identified with regard to GNAPs' originating carrier proposal. GNAPS' NXX proposal not only implies immediate access reform for any remaining intraLATA toll calls, but also, through the use of virtual NXXs, results in intraLATA toll calls being erroneously classified as local calls (through the use of originating and terminating NXX comparisons). Table 5 depicts the various intercompany compensations and end-user charges that occur under this scenario.

Table 5
Compensation Between ILECs and CLPs When They Collaborate to Complete IntraLATA Toll Calls Using Virtual NXXs
(LATA-wide Reciprocal Compensation Scenario)

ILEC Originating Call	**CLP Terminating Call**
Call viewed as Local No end-user charges if local is flat-rated	Charges the ILEC the reciprocal compensation rate

CLP Originating Call	ILEC Terminating Call
Call viewed as local Charges to end-users at the CLP's discretion	Charges the CLP the CLP's reciprocal compensation rate

In comparison with the LATA-wide scenario presented in Table 4, this scenario results in end users receiving intraLATA toll calls priced at zero. Under this scenario, the ILEC that originates an intraLATA toll call receives no additional revenues to cover the (1) costs of that call or (2) historic support for universal service. Although the ILEC receives no additional revenues, it continues to incur an additional cost for the CLP that terminates the call, which further undermines the ILEC's ability to continue to support universal service objectives. The toll avoidance GNAPs proposes results in unilateral access avoidance to an even greater degree than has ever been contemplated in any access reform proceeding—because, if GNAPs' proposal is adopted, the ILEC's originating switched access rates are not even at ***cost***, they are effectively equal to ***zero***.

It is obvious that competitive neutrality is eliminated through GNAPs' virtual NXX scheme, as no IXC can compete with a toll price of zero.

Q. WHAT OTHER ARTIFICIAL COMPETITIVE ADVANTAGES WOULD GNAPS OBTAIN BY DEFINING THE LOCAL CALLING AREA FOR RECIPROCAL COMPENSATION PURPOSES?

A. This approach is fraught with irrational outcomes. It could enable GNAPs to pay lower reciprocal compensation rates for outbound traffic and receive higher access rates for inbound traffic, or even a combination of the two.

A simple example will prove the unacceptable nature of GNAPs' proposal. Marion and Sylva are not in the same Commission-approved Verizon local calling area. But under GNAPs' originating carrier scenario, they could be in the same GNAPs local calling area. In that situation, when a Verizon Marion subscriber called a GNAPs Sylva subscriber, Verizon would be required to pay GNAPs access charges to terminate the call. However, when a GNAPs customer in Sylva called a Verizon customer in Marion, GNAPs would avoid paying Verizon's terminating access charges and instead pay only the lower reciprocal compensation rate. Thus, for identical calls between Marion and Sylva, GNAPs would collect a higher rate for calls from Verizon customers, but pay a lower rate for calls originated by its customers.

This system would inevitably encourage gaming and produce aberrant incentives that do not encourage widespread competition. GNAPs might, for example, target customers with high inbound calling, in order to collect terminating access rates for its inbound traffic (while paying Verizon the lower reciprocal compensation rate for calls between the same points).

Basing intercarrier compensation on the originating carrier's local calling areas is plainly inequitable. The direction of the call should play no part in the determining how intercarrier compensation should be assessed.

Q. IS GAMING A PARTICULAR CONCERN WITH REGARD TO GNAPS?

A. Yes. Based on Verizon's considerable experience with GNAPs in some other states, GNAPs' customer base appears to be largely limited to information service providers ("ISPs") and perhaps some other set of customers with high volumes of incoming calls

and very few outgoing calls. This very limited focus causes me to view GNAPs in a different light than a typical local carrier, and compels particular caution to avoid giving GNAPs, by regulatory fiat, opportunities for gaming and arbitrage.

Q. PLEASE ELABORATE ON HOW GNAPS' PROPOSAL WOULD UNDERMINE THE COMMISSION'S MISSION TO PROMOTE UNIVERSAL SERVICE.

A. To the extent that GNAPs can substitute reciprocal compensation payments for access charge payments, it also avoids supporting universal service. As I've explained, access charges include contributions to basic local rates, while reciprocal compensation payments do not. Thus, GNAPs' proposal to use its retail local calling area to define reciprocal compensation obligations directly conflicts with the objective of preserving and advancing universal service. There is no explicit universal service fund in North Carolina, so all state support for universal service is generated implicitly within the ILECs' rate structures—whether through switched access, toll, or other rate elements. Paying reciprocal compensation rates for what have always been designated as access traffic allows GNAPs to take implicit universal service support flows out of the system—contrary to Congress' expressed intention in § 254(d) of the Telecommunications Act of 1996 for all carriers to equitably contribute to preservation and advancement of universal service. Absolving GNAPs from contributing to maintenance of universal service also contravenes this Commission's rules, which contemplate that "[a]ll CLPs shall be willing as a condition to certification to provide support for universal service." 4 NC ADC 11.R17-1(1).

The elimination of universal service support flows from access, as well as the other harmful effects of GNAPs' proposal, will be extreme, as they cannot be limited to just the

GNAPs-Verizon relationship. If GNAPs is permitted to define away access charges through its interconnection contract, the Commission can be sure other carriers will seek to do so, as well, either through adoption of that contract or through new proceedings relying on precedent established here. Carriers with both CLP and IXC operations (as I understand GNAPs has) will be particularly interested in obtaining this ability; as the Commission knows, the IXCs' overriding policy strategy is obtaining access charge reductions. If the Commission allows CLPs to avoid access charges, traffic carried by IXCs will, either through legitimate means or misrepresentation, inevitably migrate to the local operation. The Commission should make no mistake about GNAPs' originating carrier recommendation—it is a drastic policy shift.

Q. BUT MR. LUNDQUIST CONTENDS THAT THE ISSUE IS NOT A MATTER OF POLICY, BUT "ENTIRELY ONE OF PRICING AND COMPETITIVE RESPONSE." LUNDQUIST DIRECT AT 64. WHY IS HE WRONG?

A. Verizon is not, as Mr. Lundquist argues, afraid to compete with GNAPs for LATA-wide local calling or trying to protect its revenues from legitimate competitive losses. ***If*** Verizon had the freedom to price its services as it wished (like the CLPs do) and ***if*** there were no implicit universal service subsidies in Verizon's rates, then Verizon would be happy to move its access charges toward cost, which is the effective result of GNAPs' originating carrier proposal (and its recommendation to apply reciprocal compensation to virtual NXX calls, as discussed below). But Verizon's local rates are strictly constrained by its price regulation plan and there is, as yet, no explicit funding of universal service in North Carolina. Given these constraints on Verizon's pricing, Verizon cannot compete with GNAPs on equal footing if GNAPs is permitted to define reciprocal compensation obligations on a LATA-wide (or even larger) basis. If the Commission adopts GNAPs'

proposal, Verizon's revenue losses will not be caused by its failure to successfully compete, but by the artificial regulatory advantage handed to GNAPs. Contrary to Mr. Lundquist's view, Verizon's ***pricing*** cannot be separated from the Commission's longstanding ***policies*** in this area.

Q. ARE THERE ALSO ADMINISTRATIVE PROBLEMS ASSOCIATED WITH USING THE ORIGINATING CARRIER'S RETAIL LOCAL CALLING AREA FOR RECIPROCAL COMPENSATION PURPOSES?

A. Yes. GNAPs' proposal is administratively infeasible, particularly when one considers that it cannot be limited to the Verizon/GNAPs interconnection agreement. If GNAPs convinces the Commission to accept its originating carrier proposal, GNAPs and other carriers could each have one or more retail local calling areas, which they may change any time virtually at will. Each CLP, as well as Verizon, would have to attempt to track these changes and build and maintain billing tables to implement each local calling area and associated reciprocal compensation application. Administration is further complicated if the local calling areas extends beyond LATA or state boundaries.

Aside from all the equity and policy reasons to reject GNAPs' proposal, in purely practical terms, a uniform standard must be used to determine whether a call is subject to the payment of reciprocal compensation or access charges. That standard has been and should continue to be whether the call originates and terminates within Verizon's local calling area; it brings the highest degree of competitive neutrality among ILECs, IXCs, and CLPs when assessing access or reciprocal compensation.

Q. GNAPS CLAIMS THAT "MANY STATE COMMISSIONS HAVE AGREED WITH GNAPS' POSITION ON THIS ISSUE." GNAPs PETITION AT 18. IS THAT TRUE?

A. No. As support for its position on Issue 3, GNAPs cites a Florida Commission Staff Memorandum and two California Commission decisions. GNAPs Petition n. 31.

GNAPs states that the Florida Commission Staff recommended LATA-wide reciprocal compensation in the event parties' are unable to negotiate the definition of local calling area for reciprocal compensation purposes. GNAPs claims that "Staff's position was adopted in a Public Agenda Meeting, but has not yet been released in written form by the Commission." GNAPs Petition n. 31. This statement is false. The Commission did not adopt its Staff's recommendation. Instead, it ordered further hearings to more carefully examine the most appropriate default local calling area for reciprocal compensation purposes. That hearing was held on May 8—which GNAPs knows full well because it is an active party in the proceeding.

The California Commission decisions GNAPs cites do not support its position, either. Neither decision addressed the originating carrier proposal GNAPs advances here. The September 1996 ruling did not state, as GNAPs claims, that "enhanced local calling area offerings are technologically and economically efficient." GNAPs Petition n. 31, purportedly citing Order Instituting Rulemaking on the Commission's Own Motion into Competition for Local Exchange Service, Decision No. 99-09-029, Cal. PUC LEXIS 649 *25. Rather, it stated that the Commission would not prohibit carriers from assigning virtual NXX codes "***where such an arrangement is technologically and economically efficient, and where intercarrier compensation is fairly provided.***" *Id.* The

Commission also observed that "a carrier may not avoid responsibility for negotiating reasonable intercarrier compensation for the routing of calls from the foreign exchange merely by redefining the rating designation for toll to local, *id.* at *49, which is what GNAPs seeks to do here.

GNAPs quotes the June 1996 California decision correctly, but it has nothing to do with GNAPs' originating carrier proposal in this case. In establishing ground rules for local competition, the California Commission merely affirmed that new entrants should be permitted to establish their own local calling areas, just as ILECs should be given the flexibility to propose their own optional local calling plans. Verizon, of course, does not dispute these principles.

Q. WHAT HAS REALLY BEEN THE TREND IN OTHER STATES?

A. The trend is the rejection of proposals that would circumvent the access charge regime. For example, the Ohio Commission last week rejected the same proposal GNAPs makes here, concluding that the ILECs' local calling areas "shall be used to determine whether a call is local for the purpose of local traffic termination." *Petition of Global NAPs, Inc. for Arbitration of Interconnection Rates, Terms, and Conditions and Related Arrangements with United Telephone Company of Ohio d/b/a Sprint*, Case No. 01-2811-TP-ARB and *Petition of Global NAPs, Inc. for Arbitration of Interconnection Rates, Terms and Conditions and Related Arrangements with Ameritech Ohio*, Case No. 01-3096-TP-ARB, Arbitration Award, at 11 (May 9, 2002). The Commission also explained if a virtual NXX call terminates outside of the ILEC's local calling area, it is toll or interexchange service subject to access charges. *Id.* at 8.

The Texas Public Utility Commission rejected the LATA-wide reciprocal compensation approach (proposed there by AT&T), holding that the ILEC's mandatory local calling areas were the appropriate basis for determining reciprocal compensation obligations. The Commission correctly observed that the LATA-wide proposal implicated ILEC access revenue streams and had "ramifications on rates for other types of calls, such as intraLATA toll calls," that were beyond the scope of a proceeding to address intercarrier compensation for local traffic. *Proceeding to Examine Reciprocal Compensation Pursuant to Section 252 of the Federal Telecomm. Act of 1996*, Arbitration Award, Tex. P.U.C. Docket No. 21982, 2000 Tex. PUC Lexis 95; 203 P.U.R. 4th 419 (2000).

III. ISSUE 4:

Q. HAS VERIZON PROPOSED ANY CONTRACT LANGUAGE THAT WOULD STOP GNAPS FROM ASSIGNING NXX CODES THAT ARE HOMED TO A CENTRAL OFFICE OUTSIDE OF THE CUSTOMER'S CALLING AREA?

A. No. Again, GNAPs' phrasing of the issue avoids focussing on the real dispute. Verizon has not proposed to forbid GNAPs from assigning "virtual NXX" codes, which are not associated with the rate center to which the code is homed. Rather, Verizon seeks to ensure that GNAPs pays the appropriate compensation for these non-local, virtual NXX calls. GNAPs' virtual NXX proposal presents the same themes as its proposal to define reciprocal compensation by reference to the originating carrier's local calling area. It would prevent Verizon from receiving the toll compensation and access charges it is properly due under its Commission-approved tariffs. To add insult to injury, GNAPs would bill Verizon for reciprocal compensation on virtual NXX traffic, claiming that it is local—even though these calls do not originate and terminate within the same local

calling area. So GNAPs would get a free ride for its toll traffic on Verizon's interoffice network ***and*** get paid, through reciprocal compensation, for local termination costs it does not incur.

Again, Verizon's position on this issue is not rooted in any desire to protect itself from competition, as Mr. Lundquist asserts. The same comments I made above with regard to Issue 3 apply equally here; GNAPs completely disregards the relationship between the local/toll distinction and the Commission's longstanding policy objectives, just as it ignores the constraints on Verizon's pricing. GNAPs is openly seeking an artificial competitive advantage and enhanced opportunities for regulatory gaming.

Q. BEFORE DISCUSSING THE "VIRTUAL FX" ISSUE FURTHER, PLEASE DEFINE THE TERMS RELEVANT TO THE DISCUSSION.

A. Several terms and concepts discussed in my testimony, though commonly used, are often misapplied or misunderstood. As a foundation for understanding the virtual NXX discussion, I use the following definitions:

An "**exchange**" is a geographical unit established for the administration of telephone communications in a specified area, consisting of one or more central offices together with the associated plant used in furnishing communications within that area.

An "**exchange area**" is the territory served by an exchange.

A "**rate center**" is a specified location (identified by a vertical and horizontal coordinate) within an exchange area, from which mileage measurements are

determined for the application of toll rates and private line interexchange mileage rates.

An "**NPA**," commonly known as an "area code," is a three-digit code that occupies the first three (also called "A", B and C") positions in the 10-digit number format that applies throughout the North American Numbering Plan ("NANP") Area, which includes all of the United States, Canada, and the Caribbean islands. There are two kinds of NPAs: those that correspond to discrete geographic areas within the NANP Area, and those used for services with attributes, functionalities, or requirements that transcend specific geographic boundaries (such as NPAs in the N00 format, *e.g.*, 800, 500, etc.).[1]

An "**exchange code**" is a three-digit code—also known as an "NXX," an "NXX code," a "central office code" or a "CO code"—that occupies the second three ("D, E and F") positions in the 10-digit number format that applies throughout the NANP Area.[2] Exchange codes are generally assigned to specific geographic areas. However, some exchange codes are non-geographic, such as "N11" codes (411, 911, etc.) and "special codes" such as "555." An exchange code that is geographic is assigned to an exchange located, as previously mentioned, within an area code.

When a four-digit line number ("XXXX") is added to the NPA and exchange code, it completes the 10-digit number format used in the NANP Area and

[1] *See* "NPA" in the *Glossary of the "Central Office Code (NXX) Assignment Guidelines,"* INC 95-0407-008, April 11, 2000.

identifies a specific customer located in a specific exchange and specific state (or portion of a state, for those states with multiple NPAs). This 10-digit number is also known as a customer's unique telephone number or "address."[3]

Q. WHY IS A CUSTOMER'S 10-DIGIT "ADDRESS" SIGNIFICANT?

A. A customer's telephone number or "address" serves two separate but related functions: proper call routing and rating. Each exchange code or NXX within an NPA is typically assigned to ***both a switch***, identified by the Common Language Location Identifier ("CLLI"), ***and a rate center***. As a result, telephone numbers provide the network with specific information (*i.e.*, the called party's end office switch) necessary to route calls correctly to their intended destinations. At the same time, telephone numbers traditionally also have identified the exchanges of both the originating caller and the called party to provide for the proper rating of calls—*i.e.*, the determination whether and how much the calling party should be billed for a call.

Q. CAN YOU EXPLAIN THE BASIC PRINCIPLES GOVERNING THE MANNER IN WHICH CUSTOMERS ARE CHARGED FOR THE CALLS THAT THEY MAKE?

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[2]*See* "exchange code" in the *Glossary of the "Central Office Code (NXX) Assignment Guidelines,"* INC 95-0407-008, April 11, 2000.

[3]*See* "NANP" in the *Glossary of the "Central Office Code (NXX) Assignment Guidelines,"* INC 95-0407-008, April 11, 2000.

A. Yes. One basic principle is the distinction between local calls and toll calls. The basic telephone exchange service rate typically includes the ability to make an unlimited number of calls within a confined geographic area at modest or no additional charge. This "confined geographic area" consists of the customer's "home" exchange area and additional surrounding exchanges, together designated as the customer's "local calling area." Calls outside the local calling area, with limited exceptions noted in the paragraph below, are subject to an additional charge, referred to as a "toll" or Message Telecommunications Service ("MTS") charge. "Toll" service is generally priced at higher rates, on a usage-sensitive basis, than local calling. As I explained earlier, the local/toll distinction is rooted in the decades-old public policy goal of assuring the widespread availability of affordable telephone service.

A second industry pricing convention is the principle that, generally, the calling party pays to complete a call—with no charge levied on the called party. There are a few exceptions, such as where a called party agrees to pay toll charges in lieu of applying those rates on the calling party (*e.g.*, 800/877/888-type "toll-free" service, "collect" and third-party billing, and Foreign Exchange or "FX" services).

Q. HOW DOES THE TELEPHONE NUMBER OR "ADDRESS" PLAY A ROLE IN RATING AN INDIVIDUAL CALL?

A. LECs' retail tariffs and billing systems use the NXX codes of the calling and called parties to ascertain the originating and terminating rate centers/exchange areas of the call. This information, in turn, is used to properly rate the call for purposes of billing the

calling party. If the rate center/exchange area of the called party, as determined by the called number's NXX code, is included in the originating subscriber's "local calling area," then the call is established as a "local" call. If the rate center/exchange area of the called party—again determined by the NXX code of the called number— is outside the local calling area of the caller, then the call is determined to be "toll." Thus, the rate centers of calling and called parties, as expressed in the unique NXX codes typically assigned to each rate center/exchange area, enable LECs to properly rate calls as either local or toll.

Q. WHAT IS A "VIRTUAL NXX"?

A. Whenever a CLP assigns a customer a telephone number with an NXX code designated by the carrier for a rate center/exchange area other than the one in which its customer is physically located, such an NXX is called a "virtual NXX." Indeed, the carrier may obtain an entire exchange code solely for the purpose of designating it for a rate center/exchange area in which the carrier has no customers or customers of its own or facilities to serve any customers. Instead, the CLP uses the exchange code for the sole purpose of assigning telephone numbers to its end users physically located in exchanges other than the one to which the code was assigned.

Q. HOW DOES THE EXISTENCE OF VIRTUAL NXX SERVICE AFFECT EITHER THE ROUTING OR RATING OF TELEPHONE CALLS?

A. A CLP's assignment of numbers to end users not physically located in the exchange area associated with that NXX does ***not*** affect the routing of the call from the caller to the

called party. The ILEC's network recognizes the carrier-assigned NXX code and routes the call to that carrier's switch for delivery by the carrier to its end user, the called party.

The NXX assignment does, however, affect the rating of the call. The CLP typically assigns virtual NXX codes to customers that are expected to receive a high volume of incoming calls from ILEC customers within the exchange of that NXX, and the CLP's virtual NXX arrangement allows such calls to be made without a toll charge on the calling party. In one common arrangement, a CLP allows an ISP to collocate with its switch, and then assigns that ISP telephone numbers associated with every local calling area within a broad geographic area—a LATA, or an entire state. The ISP would then be able to offer all of its subscribers a locally rated access number without having to establish more than a single physical presence in that geographic area. If the ISP had been assigned an NXX associated with the calling area in which it is located, many of those calls would be rated as toll calls.

Q. HAVE NXX CODES TRADITIONALLY BEEN USED TO GOVERN INTER-CARRIER COMPENSATION?

A. No. Any argument to the contrary confuses the rating of calls for the purpose of assessing end-user charges and treatment of calls for intercarrier compensation purposes. Before the widespread introduction of local competition following the adoption of the 1996 Act, the most important type of intercarrier compensation were the access charges that interLATA long distance carriers paid to local telephone companies. Such inter-

carrier compensation has always been governed by the originating and terminating points of the end-to-end call, not the NPA-NXX of the calling and called party.

For example, AT&T has offered customers interLATA FX service, described by the FCC as one "which connects a subscriber ordinarily served by a local (or "home") end office to a distant (or "foreign") end office through a dedicated line from the subscriber's premises to the home end office, and then to the distant end office." *AT&T Corp. v. Bell Atlantic-Pennsylvania*, 14 FCC Rcd 556, 587, ¶ 71 (1998) ("*AT&T v. BA-PA*"), *reconsideration denied*, 15 FCC Rcd 7467 (2000). An airline with a reservation office in Atlanta could provide customers in Durham a locally rated number, but all calls would still be routed to Atlanta. The FCC ruled, in that situation, that AT&T was required to pay access charges for the Durham end of that call—even though the call was locally rated for the caller, because AT&T was still using access service to complete an interLATA call to the called party. *Id.* at 590, ¶ 80. The fact that the calling party and the called party were assigned NPA-NXX's in the same local calling area was totally irrelevant to the proper treatment of the call for intercarrier compensation purposes.

Another example is "Feature Group A" access, one method that interexchange carriers ("IXCs") use to gain access to the local exchange. In that arrangement, the caller first dials a seven-digit number to reach the IXC, and then dials a password and the called party's area code and number to complete the call. Notwithstanding this dialing sequence, the service the LEC provides is considered ***interstate*** access service, not a separate local call, and the IXC must pay access charges.

Q. DOES THE PRINCIPLE THAT INTERCARRIER COMPENSATION IS GOVERNED BY THE ORIGINATING AND TERMINATING POINTS OF THE END-TO-END COMMUNICATION APPLY TO RECIPROCAL COMPENSATION?

A. Yes. The FCC has always held that reciprocal compensation does not apply to interexchange traffic, whether interstate or intrastate, but only to traffic that remains within a single local calling area. The FCC confirmed this in its April 2001 *ISP Remand Order*,[4] when it ruled that reciprocal compensation does not apply to "exchange access, information exchange access, or exchange services for such access." 47 C.F.R. § 51.701(b)(1). As the FCC has made clear, this includes all "provision of exchange services for the purpose of originating or terminating interexchange telecommunications." *ISP Remand Order at* ¶ 37 n.65. Whether a particular call is interexchange does not depend on the telephone number, it depends on whether the call remains within the local calling area or travels outside it.

Q. IS VIRTUAL NXX TRAFFIC INTEREXCHANGE?

A. Yes. There can be no dispute that virtual NXX traffic involves interexchange telecommunications. In such an arrangement, a caller located in one local calling area places a call to a called party located in a different local calling area. The manner in

[4] Order on Remand and Report and Order, *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, 16 FCC Rcd 9151 (2001) ("*ISP Remand Order*"), *remanded, WorldCom, Inc. v. FCC*, No. 01-1218 (D.C. Cir. May 3, 2002). Although the D.C. Circuit remanded the *ISP Remand Order* to permit the FCC to clarify its reading, it left the order in place as governing federal law. *See WorldCom, Inc. v. FCC*, No. 01-1218, slip op. at 5 (D.C. Cir. May 3, 2002).

which the called party's carrier assigns telephone numbers cannot change that fact, even though it does change the billing consequences for the calling party.

Q. WILL ENFORCING THE FCC'S RECIPROCAL COMPENSATION RULES WITH RESPECT TO VIRTUAL NXX TRAFFIC IMPEDE COMPETITION?

A. No. Enforcing the FCC's rules will promote competition, not impede it. GNAPs will remain free to market its virtual NXX service and receive whatever compensation for that service that its end-users are willing to pay. But Verizon should not be required to subsidize that service by paying reciprocal compensation on traffic that is interexchange. In other words, Verizon's local customers should not have to defray the costs of providing this service to end users who are located outside the exchange. Enforcing the rules will simply prevent GNAPs from exploiting a potentially lucrative regulatory arbitrage opportunity, to the detriment of competition.

Q. DO YOU AGREE THAT IT IS PROPER FOR GNAPS TO ASSIGN VIRTUAL NXX CODES TO ITS CUSTOMERS?

A. As I noted at the beginning of my discussion of this issue, GNAPs' ability to assign virtual NXX codes is not really at issue here, although preventing such assignments would avoid all of the problems I've identified. Rather, Verizon wants to ensure that the parties' agreement does not require payment of reciprocal compensation for any interexchange traffic, including virtual NXX calls. Such calls are not subject to reciprocal compensation under the FCC's rules.

Verizon believes that the issue of GNAPs' ability to assign virtual NXX codes will become a moot point if the Commission rejects GNAPs' position on compensation relative to use of these numbers. That is, if GNAPs must bear the costs it causes in making NXX assignments, and it must pay appropriate compensation for such calls, then GNAPs will have no interest in making virtual NXX assignments.

Q. DO YOU HAVE ANY OTHER CONCERNS ABOUT "VIRTUAL NXX" TRAFFIC?

A. Yes. Another concern is related to interconnection architecture. In this proceeding, GNAPs is insisting that it has a right to interconnect with Verizon at any point within a LATA and require Verizon to bear the cost of transporting traffic to that point of interconnection.

CLPs' use of virtual NXXs makes calls appear local that are actually toll service from the Verizon customer's physical location to the CLP customer's physical location, thereby denying Verizon the opportunity to collect appropriate compensation for the transport it provides to the CLPs on the call. When an ILEC's customer initiates a call to a CLP virtual NXX, the ILEC's switch sees the NXX code as being assigned to the exchange area/rate center of the originating caller or to an exchange area within the originating caller's local calling area and, therefore, does not rate the call as a toll call. In fact, the call is delivered by the CLP to its end user located ***outside*** the local calling area of the originating customer. In this situation, toll charges properly apply and would be assessed save for the assignment of virtual NXX codes. The CLP, however, does not terminate the

call within the local calling area of the originating caller. Rather, the CLP simply takes the traffic delivered to its switch and delivers the calls to its virtual NXX subscriber, often located in the same exchange as its switch—if not physically collocated with the CLP at its switch.

In short, the CLP gets a free ride for interexchange traffic on the incumbent's interoffice network. Verizon incurs essentially all of the transport costs, yet is denied an opportunity to recover its costs either from its originating subscriber or from the CLP. GNAPs, on the other hand, is compensated by its own customer for the receipt of these calls, just as an ILEC is compensated for providing a customer a traditional FX arrangement, and just as a long distance carrier is compensated for providing a customer a toll-free number. It does not make sense to require the calling party to bear the costs of this arrangement, but that is what GNAPs is seeking to achieve.

There can be little doubt why some CLPs have embraced virtual NXX service to the exclusion of other service arrangements. GNAPs should bear the cost of transporting the traffic that it receives from Verizon beyond the local calling area where that traffic originated. But GNAPs has refused to accept an agreement that would require GNAPs to bear these transport costs. Interconnection architecture issues are discussed in greater detail in the testimony of Mr. Peter D'Amico.

Q. DO YOU AGREE WITH GNAPS THAT VIRTUAL NXX SERVICE ALLOWS CUSTOMERS TO TAKE ADVANTAGE OF TECHNOLOGICAL ADVANCES GNAPS PETITION AT 20?

A. No. Virtual NXX arrangements are hardly a state-of-the-art technology and are certainly not necessary to provide customers toll-free calling. Telephone companies have been offering toll-free service for more than 20 years. The fact is that the CLP number assignment action causes originating ILECs like Verizon to treat the call at the originating switch as a local call for end-user billing and switch routing purposes. This is much like how Verizon would transport a toll call or an originating access call–existing services for which Verizon would be compensated by the originating toll user or the interexchange access customer, respectively. The only thing that's "new" here is the new scheme to manipulate intercarrier transport and compensation in a manner to shift the costs of providing this toll-free number service to the originating ILEC. There is no aspect of the virtual NXX service that would be considered new or state-of-the-art from a technological perspective.

Q. HAS THE COMMISSION ADDRESSED THIS ISSUE IN THE PAST?

A. Yes. In the arbitration between MCImetro Access and BellSouth,[5] the Commission ruled that if MCImetro interconnects with BellSouth at any point outside of BellSouth's local calling area, MCImetro should be required to compensate BellSouth for, or otherwise be

[5] Order Ruling on Objections and Requiring the Filing of the Composite Agreement, *Petition of MCImetro Access Transmission Services, LLC for Arbitration of Certain Terms and Conditions of Proposed Agreement with BellSouth Telecommunications, Inc. Concerning Interconnection and Resale Under the Telecom Act of 1996*, Docket P-474, Sub 10 (Aug. 2, 2001).

responsible for, transport beyond the local calling area. As I have noted above, the requirement that a carrier bear responsibility for transporting all calls that originate on Verizon's network outside Verizon's local calling area alleviates one significant concern associated with virtual NXX arrangements. GNAPs is directly challenging the Commission's prior ruling on this point.

In that same docket, the Commission also issued an initial ruling that calls *within a LATA* originated by BellSouth's customers to MCImetro foreign exchange customers are to be considered local for reciprocal compensation purposes.[6] BellSouth did not pose any further challenge to that ruling. I do not believe that requiring carriers to pay reciprocal compensation for virtual NXX traffic is consistent with the FCC's rules, or with this Commission's other policies.

Q. WOULD VERIZON'S POSITION RESTRICT GNAPS' ABILITY TO OFFER THIS SERVICE OR REDUCE ITS UTILITY TO GNAPS' CUSTOMERS?

A. No. GNAPs could offer the same virtual NXX service to its customers. But GNAPs could not collect reciprocal compensation for such traffic—compensation to which it has no right under the FCC's rules.

Q. HAVE OTHER STATE COMMISSIONS ADDRESSED THIS ISSUE?

A. Yes. The Florida Commission, for example, has confirmed that virtual NXX traffic is not local, and is thus not subject to reciprocal compensation, because it does not physically

[6] *Id.*

terminate in the same ILEC local calling area in which it originates.[7] Although the Florida Commission ruled that CLPs may assign telephone numbers to end users physically outside the rate center to which a telephone number is homed,[8] it agreed with its Staff's conclusion that compensation for traffic depends on the end points of the call—that is, where it physically originates and terminates—not on "the NPA/NXXs assigned to the calling and called parties."[9]

Other state commissions have barred the use of virtual NXX arrangements altogether out of concern over regulatory arbitrage. For example, in an arbitration between Focal Communications and the former Bell Atlantic-Pennsylvania, the Pennsylvania Commission reiterated its "*MFS II* directive that requires assignment of [a CLP's] customers' telephone numbers with NXX codes that correspond to the rate centers in which the customers' premises are physically located."[10] In *MFS II*, that Commission had explained its rationale as follows:

> [E]ach CLEC must comply with BA-PA's local calling areas. This is imperative to avoid customer confusion and to clearly and fairly prescribe the boundaries for the termination of a local call and the incurrence of a transport or termination charge, as opposed to termination of a toll call in

[7] *See* Staff Memorandum, *Investigation into Appropriate Methods to Compensate Carriers for Exchange Carriers for Exchange of Traffic Subject to Section 251 of the Telecommunications Act of 1996*, Docket No. 000075-TP ("Reciprocal Compensation Recommendation"), Issue 15 at 69, 71, 96 (Florida PUC Nov. 21, 2001), approved at Florida PUC Agenda Conference (Dec. 5, 2001).

[8] *Id.* at 90-96.

[9] *Id.* at 88-89.

[10] Opinion and Order, *Petition of Focal Communications Corp. of Pennsylvania for Arbitration Pursuant to Section 252(b) of the Telecommunications Act of 1996 to Establish an Interconnection Agreement with Bell Atlantic-Pennsylvania, Inc.*, Docket No. A-310630F0002, at 10-11 (Pa. PUC Jan. 29, 2001).

which case an access charge would be assessed.[11]

The Commission had addressed this issue in somewhat more detail in its initial ruling in the Focal Communications proceeding:

> With regard to BA-PA's argument that Focal escapes any obligation to pay for the use of BA-PA's transport network by assigning its customers telephone numbers with NXXs that misrepresent the actual locations of those customers, we agree with Focal that the alleged transport concerns raised by BA-PA are irrelevant in this proceeding because they are advanced as examples under an existing interconnection agreement between BA-PA and Focal, and not under the agreement that is being arbitrated. (FocalRExc., p. 17). ***At the same time, however, we are of the opinion that if the allegations by BA-PA concerning any abuse by Focal in assigning telephone numbers to customers using NXX codes that do not correspond to the rate centers in which the customers' premises are physically located are true, then we admonish Focal to comply with the directives in our MFS II Order and to refrain from this practice.*** At any rate, it is more appropriate to address the specifics of violation issues in a separate proceeding.[12]

Q. ARE YOU AWARE OF ANY OTHER STATE COMMISSIONS THAT HAVE ADDRESSED THE ISSUE OF ASSIGNMENT OF TELEPHONE NUMBERS TO END USERS LOCATED OUTSIDE OF THE RATE CENTER TO WHICH THEY ARE HOMED?

A. Yes. For example, on June 30, 2000, the Maine Public Utility Commission ordered a CLP, Brooks Fiber, to return 54 NXX codes which it was using in a "virtual NXX" capacity and rejected Brooks' proposed "virtual NXX" service. The Commission found

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[11] *Pennsylvania Pub. Util. Comm'n v. Bell Atlantic-Pennsylvania, Inc.*, R-00974176, *et al.*, 1998 WL 191237, *4 (Pa. PUC Feb. 5, 1998).

[12] Opinion and Order, *Petition of Focal Communications Corp. of Pennsylvania for Arbitration Pursuant to Section 252(b) of the Telecommunications Act of 1996 to Establish an Interconnection Agreement with Bell Atlantic-Pennsylvania, Inc.*, Docket No. A-310630F0002, at 43 (Pa. PUC Aug. 17, 2000) (citations omitted) (emphasis added).

that Brooks had no facilities deployed in any of the locations to which the 54 NXX codes were nominally assigned. As such, it rejected Brooks' arguments that it was using the codes to provide local service, and concluded that Brooks' activities had "nothing to do with local competition."[13] It found that Brooks' "extravagant" use of the 54 codes "solely for the rating of interexchange traffic" was patently unreasonable from the standpoint of number conservation.[14] The Commission further observed that Brooks' likely reason for attempting to implement an "FX-like" service, instead of a permissible 800 or equivalent service, was Brooks' "hope that it might avoid paying Bell Atlantic for the interexchange transport service provided by Bell Atlantic."[15]

Q. DOES THE FCC'S *ISP REMAND ORDER* ALLEVIATE VERIZON'S CONCERNS WITH VIRTUAL NXX?

A. The FCC's *ISP Remand Order* addresses only termination rates, and only with regard to Internet-bound traffic. It does not resolve lost toll revenue and transport cost issues associated with "virtual NXX" assignments. As I previously explained, these issues are not limited to Internet-bound traffic and are not directly related to termination rates. "Virtual NXX" assignment shifts transport costs to Verizon and makes toll calls to which toll charges properly apply appear as though they are local calls.

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[13] *Investigation Into Use of Central Office Codes (NXXs) by New England Fiber Comm., LLC d/b/a Brooks Fiber, etc., Order Requiring Reclamation of NXX Codes and Disapproving Proposed Service*, Docket Nos. 98-758 & 99-593, at 13 Tab 1 (Maine PUC June 30, 2000)

[14] *Id.* at 16.

[15] *Id.* at 12.

Q. GNAPS CLAIMS THAT THE ILECS FOREIGN EXCHANGE (FX) SERVICE IS "ESSENTIALLY A VIRTUAL NXX SERVICE." GNAPS PETITION AT 21. IS THAT TRUE?

A. No. While the two services are functionally alike from the calling party's perspective, the similarity ends there.

Verizon's FX service is a toll substitute service. It is essentially a private line service designed so that a calling party in the "foreign" exchange may place to the FX customer, located outside the caller's local calling area, what ***appears*** to be a local call. But if FX service were truly a local call, the called party would not be subject to additional charges. The called party (the FX subscriber), however, agrees to pay (on a flat-rate basis) the additional charges which the calling party would otherwise have to pay to transport the call beyond the caller's local calling area to the exchange where the FX customer's premises are located. FX service has existed for decades as a way for a customer to give the appearance of a presence in another local calling area—for example, in the local calling area of its potential customers for an FX business customer. The FX customer does so by subscribing to basic exchange service from the "foreign" switch and having its calls from that local calling area transported over either a dedicated or shared line, ***which it also pays for***, from the distant local calling area to its own premises. En route, the call is transported through the FX customer's own end office where it is connected to the customer's local loop.

When CLPs provide virtual NXX service, however, the ILEC handling the virtual NXX traffic is not compensated for transporting calls to a rate center outside the normal local

calling scope. Unlike real FX service, virtual NXX forces the originating carrier to bear the financial burden of the terminating caller's decision to provide a virtual NXX service. Instead, as I explained earlier, it tricks Verizon PA's billing systems into rating the call as local, rather than toll. In addition, for FX service, the end user customer compensates Verizon for the ability to receive calls from only ***one*** other rate center. If a customer chose to have FX service from all of the rate centers within a LATA, his total monthly FX charges would be correspondingly much greater (in order to compensate Verizon for transporting the traffic outside of the local calling area from across the LATA).

Q. HOW DOES VERIZON RECOMMEND THE COMMISSION RESOLVE THIS ISSUE?

A. The Commission should adopt Verizon's proposed contract language, making clear that reciprocal compensation does not apply to any traffic that is interexchange, defined by reference to the actual originating and terminating points of the complete end-to-end call.

IV. INTERCARRIER COMPENSATION

Q. PLEASE COMMENT ON MR. LUNDQUIST'S DISCUSSION OF "INTERCARRIER COMPENSATION ISSUES." LUNDQUIST DIRECT AT 70-78.

A. I'm not sure what GNAPs contract language this testimony is supposed to support, but Mr. Lundquist seems to be recommending that the Commission decree that TELRIC-based reciprocal compensation should apply to ISP-bound traffic if the Commission "[i]n

the event that the Commission determines at some future point that the specific intercarrier compensation rules set forth in the FCC's *ISP Remand Order* do not apply" to this traffic. Lundquist Direct at 78. Mr. Lundquist tells the Commission this action would be consistent with the findings of a report Mr. Lundquist and his colleague submitted to the FCC (but which was not filed with the North Carolina Commission) and with the Commission's "previous findings" that ISP-bound traffic is local. *Id.*

The Commission should not waste any time considering this odd and obviously inappropriate recommendation. The *ISP Remand Order* (which remains in effect) makes clear that state Commissions have no jurisdiction over ISP-bound traffic. So GNAPs is asking the Commission to engage in the pointless exercise of devising a scheme it clearly has no authority to impose.

Although Mr. Lundquist's recommendation is not useful to resolving any issue in this interconnection arbitration, it does serve to highlight GNAPs' motivations and its lack of interest in engaging in legitimate local competition. Amazingly, GNAPs continues to believe that the arbitrage engendered by explicit reciprocal compensation for ISP-bound traffic was a positive development, rather than the serious problem the FCC identified in its *ISP Remand Order*. GNAPs openly disagrees with the FCC's conclusion that the intercarrier compensation mechanism under which the originating carrier pays the carrier serving the ISP "created opportunities for regulatory arbitrage and distorted the economic incentives related to competitive entry into the local exchange and exchange access markets." *ISP Remand Order* at ¶ 2. GNAPs obviously wishes the gravy train of

reciprocal compensation for ISP-bound traffic were still running, but wishing cannot supersede federal law and sound policy. Mr. Lundquist's observations on this matter confirm the critical importance of rejecting any contract language that would give GNAPs enhanced arbitrage and gaming opportunities, to the detriment of fair and efficient local competition.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.